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C O N F I D E N T I A L SECTION 01 OF 03 BRATISLAVA 000274

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TAGS: [ENRG](#) [ECON](#) [EPET](#) [LO](#) [RU](#)

SUBJECT: PROGRESS ON TRANSPETROL NEGOTIATIONS

REF: A. PRAGUE 340

[1](#)B. BRATISLAVA 161

[1](#)C. BRATISLAVA 160

[1](#)D. BRATISLAVA 35

Classified By: Ambassador Vincent Obsitnik for Reasons 1.4 b) and d)

[11.](#) (C) Summary: The Slovak government is moving forward with discussions to buy back the 49 percent stake in the Transpetrol oil pipeline from Netherlands-based Yukos Finance. Both sides have completed valuations and are scheduled to begin pricing negotiations on June 17 in London. A few legal complications remain, but for the time being the Ministry of Economy is focused on reaching a commercial agreement. Rumors have appeared in the press since Russian PM Zubkov's visit in April that the GOS will resell the shares to a Russian company once it is successful in buying them back. Post does not have any confirmation of such an agreement, and there are several solid arguments against such a sale, not the least of which is PM Fico's strong desire to get strategic energy assets back under government control. Nevertheless, if pushed, the GOS might give in to Russians demands, especially if the sale is linked with ongoing gas negotiations with Moscow. End Summary

GOS SERIOUS ABOUT COMPLETING A DEAL FOR TRANSPETROL

[12.](#) (C) The Slovak government remains committed to buying back the 49 percent stake plus management control of Transpetrol from Yukos Finance (Reftel D). Government officials have expressed this sentiment both publicly and in private on numerous occasions in recent months. Economy Minister Lubomir Jahnatek met with Yukos Finance Directors Bruce Misamore and Dave Godfrey on March 6 in Washington DC, the first time the two sides had gotten together at this level since August [12](#)006. Based on the agreement from this meeting, each side has completed its own valuation to determine the base price for starting negotiations. They exchanged the completed valuations in mid-May, and are now scheduled to meet in London on June 17 to begin negotiations over the price.

[13.](#) (C) Wood and Company, the Prague-based consulting firm contracted by the GOS for the pricing study, came up with a recommended price range of USD 180 to 200 million. This is well below the base estimate of USD 270 to 280 from Muse Stancil, the Texas-based firm hired by Yukos Finance to value the asset. The two consulting companies are meeting in advance of the June 17 discussions to see if they can bring the valuations closer by agreeing on some common reference points (on data, methodologies, etc), which should partially bridge this gap.

[14.](#) (C) Yukos Finance argues that the significant appreciation of the Slovak Koruna (Note: the value of the 49 percent stake has increased from USD 74 million when sold in 2002 to USD 178 million today as the exchange rate has gone from SKK/USD 47 to 19.5) along with the accumulation of unpaid dividends of USD 27 million and higher tariff rates justifies a price

well-above USD 200 million. Godfrey and Misamore will also make the case that there are real opportunities to increase volumes over the medium-term, specifically by connecting Transpetrol to the Schwechat refinery in Austria. The GOS takes a more pessimistic view, stressing that volumes dropped in 2007 to 10.64 MT from 11.15 MT the previous year. They argue that an extension to Schwechat should not be included in the price since it has been blocked for several years due to environmental concerns and ultimately depends on a GOS decision to go forward with such a deal. (Comment: Although both sides will put forward arguments in favor of their respective negotiating positions, at the end of the day it will be hard for either to walk away from the table. Yukos Finance has repeatedly threatened to hold an auction if it could not reach a deal with the GOS, but the GOS will regain management control no matter who buys the stake (based on the Shareholder's agreement), and Jahnatek has promised to challenge any sale to a third party in the courts. The GOS has several reasons for wanting to regain control, as outlined in para 7 below, and has consistently opposed a sale to any third party that is not also an oil supplier. End Comment)

LEGAL COMPLICATIONS SECONDARY TO GETTING A DEAL

¶5. (C) The GOS restarted negotiations with Godfrey and Misamore when it became clear that these American Directors of Yukos Finance, which is registered in the Netherlands, had the most legitimate claim to the asset due to a favorable court ruling in Amsterdam in October. (Reftel D). Despite additional court rulings in favor of Godfrey and Misamore in March, they have not been able to get their names reinstated

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on the Dutch Commercial registry as the legal representatives of Yukos Finance. This could be an impediment to completing negotiations since the GOS claims that it can only do a deal with the designated representatives of Yukos Finance. Yukos Finance representative and Transpetrol board member Jan Kridla told EconOff that he expects the issue to be resolved in the next few weeks, a claim he has made numerous times since last November.

¶6. (C) Monte Valle, an American-led investment group that purchased Yukos Oil's claim to Yukos Finance in an August 2007 auction in Moscow for USD 305 million, reportedly sent a letter to PM Fico in April requesting that the GOS halt negotiations with Godfrey and Misamore. Monte Valle is reportedly becoming increasingly desperate after the October Dutch court decisions returning control to Godfrey and Misamore and several unsuccessful attempts to overturn this decision. There is no evidence that the GOS has met with Monte Valle representatives or plans to halt negotiations.

RUSSIAN INTEREST IN TRANSPETROL

¶7. (C) During former Russian PM Zubkov's visit to Bratislava in early April Russian media reported that he and Fico had agreed that the GOS would sell the 49 percent stake in Transpetrol to a Russian company after completing a deal with Yukos Finance (Reftel C.) In numerous conversations with a full range of contacts in the energy sector, including top GOS officials and others involved in negotiations, Post has consistently received the message that there was no indication that Fico had agreed to such a deal. (Note: This differs from the recent statements by Czech Government representatives, as outlined in Reftel A.) There are several reasons for the strong GOS preference for regaining 100 percent control over Transpetrol:

-- Buying back the 49 percent stake has been a top objective since Fico came to power in 2006, which he and Jahnatek have consistently made clear in both public and private comments over the past two years. Fico strongly opposed the previous government's privatization of energy assets, and would like to reinstate greater state control in the energy sector.

Transpetrol is one of the few assets that he can again control.

-- From mid-2006 to mid-2007 the Russian government pressured the GOS to allow them to purchase the 49 percent stake. The GOS carefully avoided Russian attempts to gain control, including not approving Russian nominees to the Transpetrol board in November 2006 when there were competing claims as to who controlled Yukos Finance. Slovak officials have made it clear throughout that their preference is a GOS buyback, but have acknowledged in the past that if pressured they may have to sell a minority stake to Russia. Regaining management control has remained non-negotiable. (Note: GOR pressure on Slovakia seemed to end with the sale to Monte Valle last August. Until the media rumors in April, we were not aware of any attempts by the GOR to push for a sale to Russian interests. In fact, Jahnatek claimed this past January that he had GOR approval to continue negotiations with Yukos Finance. End Note)

-- An Eastern Slovak businessman, Ignac Ilcisin, has an ownership claim to 34 percent (or two-thirds of the Slovak government's 51 percent stake) of Transpetrol. The dispute has been caught up in the courts since the late 1990s. In 2006 the Supreme Court decided against Ilcisin, but a Constitutional Court ruling this past March overturned this decision and sent the case back to the Supreme Court. Economy State Secretary Peter Ziga told Econoff in April that the GOS remains confident that the final verdict will go in its favor, but it is nevertheless a risk. According to the Transpetrol Shareholder's Agreement, if the GOS lost two-thirds of its 51% stake it would be required to give Yukos Finance an additional two percent, which would give them both management and ownership control.

-- According to Chair of the Parliamentary Economic Committee, Maros Kondrot, if the GOS controls 100% of the pipeline, then Slovakia can count the oil in the pipeline towards its EU-mandated reserve requirements, which would save the government from having to build additional storage facilities. Kondrot has been one of the strongest advocates in favor of buying back the 49 percent stake.

¶8. (C) The Director of International Economic Cooperation at the Ministry of Foreign Affairs, Jaroslav Chlebo, traveled to Moscow last month for bilateral energy discussions. Chlebo told EmbOffs last week that GOR representatives had said Russia could only guarantee the flow of oil along the Druzhba

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over the medium term, which Chlebo defined as approximately 15 years. He took this as a clear message that the GOS needs to pursue alternative supply routes. (Note: The GOR confirmed during these meetings that Russia would continue to supply gas to Slovakia and Western Europe on the "Brotherhood" pipeline over the long-term.).

BATCHING CASPIAN CRUDE ON THE DRUZHBA

¶9. (C) Ukrainian efforts to initiate a one-day test batch of 40,000 tons of Caspian crude from Brody in Ukraine to the Kralupy refinery in the Czech Republic finally appear to be moving forward after having been put off due to repeated concerns by Transpetrol (Reftel B). The Slovak government supports the project, but Transpetrol has had a number of technical and contractual issues that held up its approval. UkrTransNafta representative in Slovakia Mikulas Rakovsky told EconOff June 10 that all of the outstanding issues relating to the trial have now been resolved, the last of which was measurement discrepancies between Czech pipeline operator Mero and Transpetrol. UkrTransNafta has essentially agreed to cover all costs and bear the risks associated with the trial. With these commitments in place, Transpetrol has said that it will sign the agreement in the next week. Rakovsky does not expect the trial to take place until September at the earliest, because several additional

agreements need to be signed, the Caspian crude must be purchased, and Kralupy requires at least 45 days notice to accept the shipment.

COMMENT

¶10. (C) The GOS remains motivated to buy back the 49 percent Transpetrol stake and has taken the necessary steps in recent months to put itself in the position to complete a deal with Yukos Finance. Price will be an important factor, as much for the political perception as the budgetary impact, but that is the case in any commercial negotiation. The GOS would like to maintain control over Transpetrol, and recognizes that efforts such as the trial to batch Caspian crude are in the country's long-term interest. Nevertheless, the Slovak Gas Company is currently negotiating a long-term gas project with Gazprom beginning in 2009, and Jahnatek and other GOS officials would likely be susceptible to Russian pressure linking Transpetrol with the gas negotiations. If this were this were the case, then the GOS would push to at least maintain management control. The option of a sale to a third party (other than Russia) has been, and likely will remain, a non-starter for the Slovaks. End Comment.

OBSITNIK